

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

**MANAGEMENT OF THE GENERAL RESERVE OF
INDUSTRIAL PLANT EQUIPMENT**

Report No. 93-070

March 19, 1993

Department of Defense

The following acronyms are used in this report.

DIPEC.....Defense Industrial Plant Equipment Center
DLA.....Defense Logistics Agency
GSA.....General Services Administration
IPE.....Industrial Plant Equipment



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202

March 19, 1993

MEMORANDUM FOR ASSISTANT SECRETARY OF DEFENSE (PRODUCTION AND
LOGISTICS)
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit Report on the Management of the General
Reserve of Industrial Plant Equipment (Report
No. 93-070)

We are providing this final report for your information and use. This report resulted from our expanded review of Government property initiatives related to the general reserve of industrial plant equipment at the Defense Industrial Plant Equipment Center, Memphis, Tennessee.

Comments received on a draft of this report conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the audit staff. If you have any questions on this audit, please contact Mr. Richard B. Jolliffe, Program Director, at (703) 692-2999 (DSN 222-2999), or Mr. Garry A. Hopper, Project Manager, at (703) 692-3321 (DSN 222-3321). The planned distribution of this report is listed in Appendix D.

A handwritten signature in black ink, reading "Robert J. Lieberman", is positioned above the typed name.

Robert J. Lieberman
Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

**Report No. 93-070
(Project No. OCA-0047.01)**

March 19, 1993

MANAGEMENT OF THE GENERAL RESERVE OF INDUSTRIAL PLANT EQUIPMENT

EXECUTIVE SUMMARY

Introduction. The Defense Industrial Reserve Act authorized a general reserve of industrial plant equipment to be maintained in ready-for-issue condition for national emergencies. The reserve is managed by the Defense Industrial Plant Equipment Center, Memphis, Tennessee, and consists of 11,883 items with an acquisition value of \$263,429,989. As of December 8, 1992, 56 percent of this equipment was in storage and 44 percent was on loan.

Objectives. Our objectives were to evaluate the management of the general reserve of industrial plant equipment related to the disposal of excess equipment and to determine the effectiveness of applicable internal controls.

Audit Results. The Defense Industrial Plant Equipment Center did not report 3,300 items of excess industrial plant equipment to the General Services Administration for disposal; this equipment was on loan to schools. If the excess plant equipment was either donated to the schools or sold, monetary benefits would result.

Internal Controls. No material internal control deficiencies were identified during the audit. See details in Part I for a discussion of controls assessed.

Potential Benefits of Audit. The DoD can realize monetary benefits estimated at \$240,000 over 6 years in reduced administrative expenses from direct donation of excess industrial plant equipment in lieu of retaining excess items. Appendix B summarizes potential monetary and other benefits from either direct donation or sale of the industrial plant equipment.

Summary of Recommendation. We recommended that the Director, Defense Logistics Agency, either report excess industrial plant equipment on loan to schools to the General Services Administration for disposal or request Congress to allow direct donation to schools.

Management Comments. The Defense Logistics Agency concurred in the recommendation to request approval for direct donation of the industrial plant equipment. The Defense Logistics Agency agreed to make the equipment donation issue a part of the Defense Logistics Agency legislative package each year until Congress

resolves it. In addition to the students benefiting from use of the equipment, the Defense Logistics Agency estimated that direct donation would eliminate approximately \$40,000 annually in administrative expenses for monitoring the items on loan. We have retained the alternative recommendation in the final report, because the request to donate the excess items requires congressional action. A full discussion of management comments is in Part II and the complete text of management comments is in Part IV of this report.

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This report was prepared by the Contract Management Directorate, Office of the Assistant Inspector General for Auditing, DoD. Copies of the report can be obtained from the Secondary Reports Distribution Unit, Audit Planning and Technical Support Directorate, (703) 614-6303 (DSN 224-6303).

PART I - INTRODUCTION

Background

The Defense Industrial Plant Equipment Center (DIPEC), Memphis, Tennessee, was established in 1962 as a primary field-level activity under the Defense Logistics Agency (DLA). DIPEC manages a general reserve of industrial plant equipment (IPE); provides maintenance, technical, and contract support for DoD activities regarding IPE; acts as the DoD clearinghouse for IPE; and oversees the central inventory of DoD-owned IPE.

Appendix A summarizes United States Code, title 50, section 451, "The Defense Industrial Reserve Act," which authorizes DIPEC to maintain a defense industrial reserve, or general reserve, as part of the total industrial base. The general reserve provides a pool of industrial machine tools and other industrial manufacturing equipment to supply DoD needs in a national emergency. The Act states that the general reserve shall not exceed the minimum requirements needed in a national emergency.

A November 1986 Under Secretary of Defense for Acquisition memorandum detailed specific property initiatives (the Initiatives) for DoD activities to accomplish. Two initiatives required DIPEC to review all IPE in the general reserve and retain only essential equipment in a ready-for-issue condition.

Objectives

The objectives of this audit were to evaluate the management of the general reserve related to the disposal of excess IPE and to determine the effectiveness of applicable internal controls. During our overall review of the Initiatives, we found that DIPEC was not reporting identified excess IPE to the General Services Administration (GSA) for disposal. Therefore, we performed a review of DIPEC management of the general reserve of IPE.

Scope

Scope of review. The audit covered DIPEC procedures and practices for managing the general reserve of IPE and implementing the Initiatives. As of December 8, 1992, the general reserve consisted of 11,883 items of IPE with an acquisition value of \$263 million. Of the total, 6,642 items were in storage and 5,241 items were on loan. We reviewed the IPE inventory reconciliation report and related documents for assets in storage and on loan. We tested the reliability of computer-generated data as part of our review. Although we found deficiencies, we considered the data to be accurate and reliable for our primary purpose of identifying excess IPE. The activities visited or contacted during the audit are listed in Appendix C.

Audit period and standards. This economy and efficiency audit was made from January through December 1992 in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD. Accordingly, we included such tests of internal controls as were considered necessary.

Internal Controls

The audit evaluated internal controls covering DIPEC policies and procedures for disposing of excess IPE. The internal controls applicable to disposal of excess IPE were deemed to be effective in that no material deficiencies were disclosed by the audit.

Prior Audits and Other Reviews

Inspector General, DoD, Audit Report No. 93-037, "Government Property in the Possession of Contractors," December 17, 1992, reviewed implementation of the November 1986 Under Secretary of Defense for Acquisition property initiatives. The audit showed the Initiatives for developing policy, revising regulations, and establishing procedures were basically implemented by the Military Departments and DLA; however, DoD field activities had only partially implemented or not implemented the Initiatives related to the identification and disposal of unneeded property, storage of property, and the general management of Government property. DoD issued guidance that should correct the observed deficiencies. Therefore, no recommendations were made.

Inspector General, DoD, Inspection Report, "Defense Industrial Plant Equipment Center," August 7, 1986, indicated that the Air Force air logistics centers reported their IPE assets to DIPEC in summary form by national stock number instead of on an individual basis, as done by the other Military Departments. Inadequate reporting created a problem because inaccurate data might have been provided when DIPEC reported the total assets in the industrial base. DLA and the Air Force concurred with the finding and agreed to take action to identify the data required by DIPEC.

General Accounting Office Audit Report No. NSIAD-93-8 (OSD Case No. 9156), "Property Management: DoD can Increase Savings by Reusing Industrial Plant Equipment," November 6, 1992, reviewed the purchase, reutilization, and disposal of IPE by DIPEC. The report stated that the Military Departments can sell a Government-owned, contractor-operated plant as a package even though that plant contains equipment that may be needed elsewhere in the DoD. As a result, the Government may have to purchase replacement equipment. The DoD partially agreed with the report findings. The DoD agreed to report IPE for reutilization screening during plant sales negotiations, if the IPE becomes excess to requirements.

PART II - FINDING AND RECOMMENDATION

DISPOSAL OF EXCESS EQUIPMENT

DIPEC had not disposed of IPE that was identified as potential excess to DoD requirements for the general reserve. The excess equipment was not disposed of because DIPEC did not notify GSA that 3,293 items of potential excess IPE were on loan to schools. As a result, IPE, with an estimated potential cash collection value of up to \$1.7 million, was not being processed for sale.

DISCUSSION OF DETAILS

Background

The Defense Industrial Reserve Act (the Act) requires DIPEC to dispose of excess items as expeditiously as possible. The Act, however, allows DoD to lend essential IPE from the general reserve to non-profit educational institutions or training schools, such as high schools, provided that the schools return the equipment when requested by DoD.

Property on Loan

As of December 8, 1992, 3,293 items of potential excess plant equipment were loaned out to schools. The items are recorded on DLA's financial statements at acquisition value. The items should be disposed of in accordance with existing regulations. The Defense Federal Acquisition Regulation Supplement requires notification to GSA when IPE becomes excess. The Administrator, GSA, is responsible for screening and disposing of the excess equipment. DIPEC and DLA representatives would prefer to donate the IPE directly to the schools; however, Federal Acquisition Regulation 45.609, "Donations," specifies that donation of surplus property is subordinate to any need for property by a Federal agency. DIPEC officials had not taken any action to notify GSA of excess items because they believed the schools needed the items.

Based on the original acquisition cost of the 3,293 excess items on loan to schools, and the relative fair market value of IPE, we estimated that the U.S. Treasury could obtain up to \$1.7 million from sale of these items. See Appendix B for the methodology used to calculate monetary benefits.

If it is good public policy to continue the present practice of leaving the potential excess IPE with the schools, then this practice should be legitimized through a change in the law. Specifically, the law should be modified to provide for direct donation to schools.

RECOMMENDATION, MANAGEMENT COMMENTS, AND AUDIT RESPONSE

We recommend that the Director, Defense Logistics Agency either:

1. Notify the General Services Administration of 3,293 items of industrial plant equipment on loan to schools that are excess to DoD requirements, or

2. Request Congress to change United States Code, title 50, section 451 to allow the Defense Logistics Agency to donate excess industrial plant equipment directly to the schools in possession of the equipment.

Management comments. The Deputy Director, DLA, concurred with the recommendation to request congressional action to permit direct donation of excess industrial plant equipment to schools. DLA will make it part of DLA legislative requests. However, DLA stated that the direct donation issue was not new and that attempts were previously made to change the law. Donation is the desirable alternative because the equipment is of great benefit to the students of the schools and if the items were declared excess the schools must ship the items to a DLA activity at their own expense. DLA estimated potential monetary benefits of \$40,000 annually that will result from reduced administrative expenses associated with record keeping of excess industrial plant equipment.

Audit response. We consider DLA comments to be responsive and accept the DLA estimate of monetary benefits for reduced administrative expenses. We have retained the alternate recommendation in the final report, because the request to donate the excess items requires congressional action. Accordingly, if Congress does not authorize direct donation, then DLA should report to GSA the excess industrial plant equipment.

PART III - ADDITIONAL INFORMATION

APPENDIX A - Background on Defense Industrial Plant
Equipment Center

APPENDIX B - Summary of Potential Benefits Resulting from Audit

APPENDIX C - Activities Visited or Contacted

APPENDIX D - Report Distribution

APPENDIX A - BACKGROUND ON DEFENSE INDUSTRIAL PLANT EQUIPMENT CENTER

The Defense Industrial Reserve Act is codified at 50 U.S.C. 451. The term "defense industrial reserve" (general reserve) is defined, in part, as a general reserve of industrial manufacturing equipment, including machine tools, selected by the Secretary of Defense for retention for national defense or for other emergency use. The Act states, in part, that:

...such reserve shall not exceed in number or kind the minimum requirements for immediate use in time of national emergency, and that any such items which shall become excess to such requirements shall be disposed of as expeditiously as possible....

The Act further authorizes the Secretary of Defense to:

(6) authorize the disposition in accordance with existing laws of any of such property when in the opinion of the Secretary such property is no longer needed by the Department of Defense; and

(7) authorize and regulate the lending of any such property to any nonprofit educational institution or training school whenever (A) the program proposed by such institution or school for the use of such property will contribute materially to national defense, and (B) such institution or school shall by agreement make such provision as the Secretary shall deem satisfactory for the proper maintenance and care of such property and for its return, without expense to the Government, upon request of the Secretary.

APPENDIX B - SUMMARY OF POTENTIAL BENEFITS RESULTING FROM AUDIT

<u>Recommendation Reference</u>	<u>Description of Benefit</u>	<u>Amount and/or Type of Benefit</u>
1.	Program Results. Sale of excess IPE.	Funds put to better use through a one-time collection of up to \$1.7 million to U.S. Treasury.
2.	Program Results. Request Congressional permission to donate excess industrial plant equipment. Reduced administrative expense by eliminating record keeping.	Funds put to better use through reduced administrative expense estimated at \$240,000 over 6 years.

Potential Monetary Benefits Calculation

We estimated the potential monetary benefits for excess IPE on loan by multiplying the acquisition cost by a ratio. The information was obtained from DLA on sales of IPE by the Defense Reutilization and Marketing Office. The ratio (sales/original acquisition cost) was used to estimate the relative fair market value of the excess IPE. We estimated the cash collection to be up to \$1.7 million.

Original acquisition cost	\$16,955,501
Ratio	<u>x .10</u>
Estimated cash collection	<u>\$ 1,695,550</u>

APPENDIX C - ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Office of the Under Secretary of Defense for Acquisition,
Washington, DC
Office of Assistant Secretary of Defense (Production and
Logistics), Washington, DC

Department of the Navy

Office of the Assistant Secretary of the Navy (Research,
Development, and Acquisition), Washington, DC

Department of the Air Force

Aeronautical Systems Division, Air Force Systems Command,
Wright-Patterson Air Force Base, OH

Defense Activities

Headquarters, Defense Logistics Agency, Alexandria, VA
Defense Industrial Plant Equipment Center, Memphis, TN
Defense Industrial Plant Equipment Facility, Atchison, KS
Defense Industrial Plant Equipment Center, Stockton, CA
Defense Industrial Plant Equipment Center, Mechanicsburg, PA
Defense Contract Management Command, Alexandria, VA
Defense Plant Representative Office, General Electric
Aircraft Engines, Cincinnati, OH

APPENDIX D - REPORT DISTRIBUTION

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition
Director of Defense Procurement
Assistant Secretary of Defense (Production and Logistics)
Comptroller of the Department of Defense

Department of the Army

Secretary of the Army
Inspector General, Department of the Army
Auditor General, Army Audit Agency

Department of the Navy

Secretary of the Navy
Assistant Secretary of the Navy (Financial Management)
Auditor General, Naval Audit Service

Department of the Air Force

Secretary of the Air Force
Assistant Secretary of the Air Force (Financial Management and
Comptroller)
Auditor General, Air Force Audit Agency

Defense Activities

Director, Defense Logistics Agency
Director, Defense Industrial Plant Equipment Center

Non-Defense Federal Activities

Office of Management and Budget
National Security and International Affairs Division, Technical
Information Center, General Accounting Office

Chairman and Ranking Minority Member of Each of the Following
Congressional Committees and Subcommittees:

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Operations
House Subcommittee on Legislation and National Security,
Committee on Government Operations

PART IV - MANAGEMENT COMMENTS

Defense Logistics Agency

DEFENSE LOGISTICS AGENCY COMMENTS



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304-6100



PROPERTY
DEFENSE DLA-CI

22 FEB 1993

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING,
DEPARTMENT OF DEFENSE

SUBJECT: Draft Audit Report on the Management of the General
Reserve of Industrial Plant Equipment (Project No.
OCA-0047.01)

This is in response to your 31 December 1993 request.

2 Encl

Jacqueline G. Bryant
JACQUELINE G BRYANT
Chief, Internal Review Division
Office of Comptroller

cc:
DLA-O
DLA-LX

DEFENSE LOGISTICS AGENCY COMMENTS (cont'd)

TYPE OF REPORT: AUDIT

DATE OF POSITION: 22 FEB 83

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on the Management of the General Reserve of Industrial Plant Equipment (Project No. OCA-0047.01)

FINDING: DIPEC has not disposed of IPE that was identified as potential excess to DoD requirements for the general reserve. This condition occurred because DIPEC did not notify GSA that 3,293 items of potential excess IPE were on loan to schools. As a result, IPE, with an estimated potential cash collection value of up to \$1.7 million, was not being processed for sale.

DLA COMMENTS: Concur in the finding; however, this is not a new issue. Legislative action to correct this problem, by permitting the Secretary of Defense to donate excess IPE directly to the school that was originally loaned the equipment, has been pursued on several occasions (Senate Bills S.2038 (introduced by then Senator Quayle in February 1982), S.601 in February 1983, and most recently in September of 1991).

The Tools for Schools program authorized by PL 93-155, and earlier by PL 80-883, has high visibility and support throughout the national education system, OSD, and the Congress. When government property on loan to vocational schools and other educational institutions is declared excess to DoD requirements, current procedures require that the schools ship such items to the Defense Reutilization and Marketing office at their own expense. The schools are also responsible for transfer fees imposed by State Agencies, and for the cost of insurance required on Government-owned property. The shipping, transfer, and insurance costs along with the schools' concern of retaining the equipment loaned to them after the equipment has been determined to be excess to DoD requirements, impact negatively on DoD's ability to ensure the continued success of the program. Direct donation would eliminate the shipping, transfer, and insurance fees described above.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:

- (x) Nonconcur. (Rationale must be documented and maintained with your copy of the response.) As stated above, this is not a new issue, nor is it a management control weakness. It has been known and pursued since 1982.
- () Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
- () Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Nancy Johnson, DLA-OSP, x47975, 2/3/83

PSE REVIEW/APPROVAL: James J. Grady, Jr., Deputy Executive Director, Directorate of Supply Operations, DLA-O, x46102

DLA APPROVAL:



LAWRENCE P. FARRELL, JR.
Major General, USAF
Deputy Director

DEFENSE LOGISTICS AGENCY COMMENTS (cont'd)

Final Report
Page No.

TYPE OF REPORT: AUDIT

DATE OF POSITION: 22 FEB 1993

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on the Management of the General Reserve
of Industrial Plant Equipment (Project No.
OCA-0047.01)

RECOMMENDATION 1.a. (page 9): We recommend that the Director, Defense
Logistics Agency, either notify the General Services Administration of
3,293 items of industrial plant equipment on loan that are excess to DoD
requirement, or

RECOMMENDATION 1.b. Request Congress to change United States Code, title
50, section 451 to allow the Defense Logistics Agency to donate excess
industrial plant equipment directly to the schools in possession of the
equipment.

DLA COMMENTS: Concur with recommendation. DLA concurred in a DoD
legislative proposal, (Misc 2384 "To permit DoD donation of items on loan
under DIPEC 'Tools for Schools' programs.") in December 1992. We will
make this issue a part of the DLA legislative package each year until it
is resolved. This action is closed for reporting purposes.

DISPOSITION:

- () Action is ongoing. Estimated Completion Date:
- (X) Action is considered complete.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:

- (X) Nonconcur. (Rationale must be documented and maintained with
your copy of the response.) SAME AS ABOVE
- () Concur; however, weakness is not considered material. (Rationale
must be documented and maintained with your copy of the response.)
- () Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

MONETARY BENEFITS: Approximately \$40,000 annually.

DLA COMMENTS: The government would benefit from direct donation by
reduced record keeping for administering loans for items which have no
potential benefit to the DoD.

ESTIMATED REALIZATION DATE: UNKNOWN


AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: Nancy Johnson, DLA-OSP, x47975, 2/3/93

PSE REVIEW/APPROVAL: James J. Grady, Deputy Executive Director,
Directorate of Supply Operations, DLA-OD, x46102

DLA APPROVAL:


LAWRENCE P. FARRELL, JR.
Major General, USAF
Deputy Director

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AUDIT TEAM MEMBERS

David K. Steensma, Director, Contract Management Directorate
Richard B. Jolliffe, Audit Program Director
Garry A. Hopper, Audit Project Manager
Gerald L. Werking, Audit Team Leader
Dorothy L. Jones, Auditor
Christine S. Bowles, Auditor
Margaret R. Kanyusik, Editor
Velma L. Booker, Administrative Support